DOW THEORY LETTERS INC.

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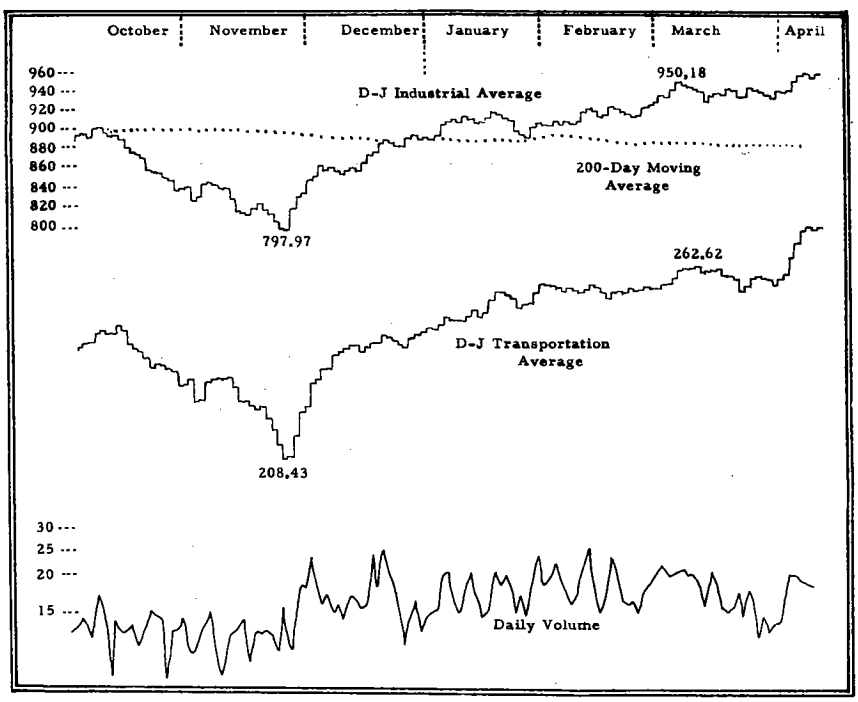
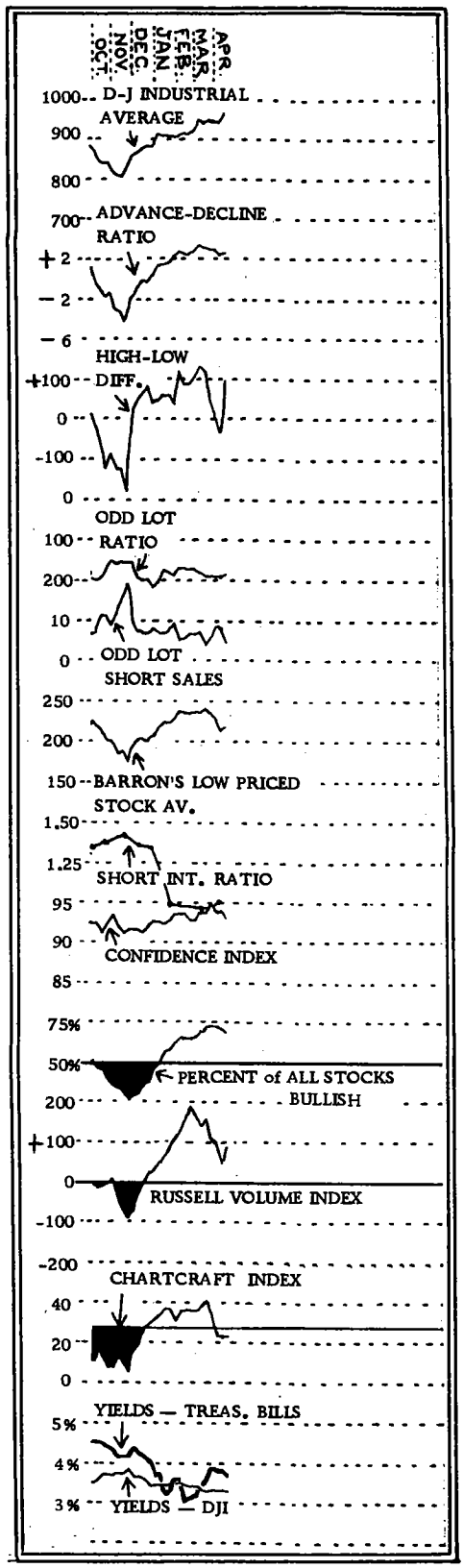
THE MARKET: Everybody wants to go to the party. For instance, starting this month the state of Connecticut will begin investing state pension and retirement funds in common stocks in a massive switch in investment policy which, it is hoped, will have the Connecticut funds in an ultimate 50% position in common shares. All over the nation other funds and pension plans are eyeing the market with hungry eyes, both because inflation is wiping out their saving and buying power and because the market has been heading up long enough to arouse their instincts of greed. A third reason for the switch is the debasement of the dollar itself, a phenomenon which makes it that much easier for the man who is spending someone else's money to say, "Well, the blasted green stuff is worth less every week so who can blame me for swapping it for corporate certificates! If I'm wrong, the rest of the country and Government will be just as wrong as I am. Besides, the Government is underwriting the inflation and using it as an instrument of policy, so why should I fight it?"

And in truth, those are pretty persuasive arguments, although there's nothing particularly new or original in them. The same thinking (with modifications) has been heard at or near all important market tops, the most notable being that of 1929. Today's era differs from all others in the sheer size of the situation. For instance, the 1929 crash, which brought on the greatest volume in stock market history, was ushered in on 16 million shares (October 29). Today, it's a dull day when we have less than 16 million shares traded on the N.Y.S.E. It isn't that the U.S. population has doubled since 1929 (it hasn't), but that far more people are now busy with the stock markets.

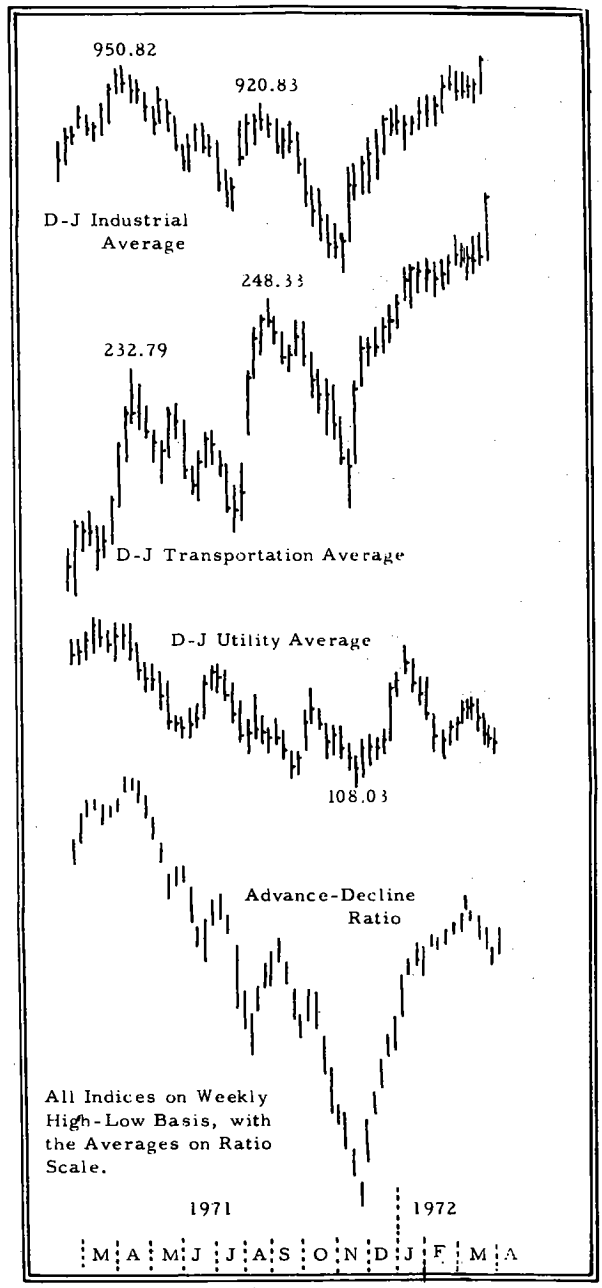
The second major difference is that today our Government is using all forms of communications in an attempt to "bull" the markets, this being a definite





strategy for political power. Mr. Nixon knows that good times on Wall Street constitute a major plus in his election campaign and so far he has stopped at nothing (even switching his economic philosophy) in his headlong drive to win again in fall, 1972. Thus the market has to deal with massive public participation and a Government which is using every form of propaganda and communications to get Wall Street roaring on the upside.

These are some of the reasons why I find the whole situation utterly fascinating. For here we are, watching the famous D-J Industrial Average move into the 950-995 area again, a movement set off by monumental Administration efforts to send the market and the economy into orbit no matter what the costs, no matter what the consequences. Of course, the crucial question is whether (with all this stimulation) the Dow Industrials will push up and over their 1966 bull market peak of 995.15, thus labeling Mr. Nixon the Prince of Prosperity. Or whether Wall Street will simply use the Administration's efforts as a vehicle for distribution, cynically offering the hope of a jaunt "above 1000" as a lure to get rid of stock at high prices?

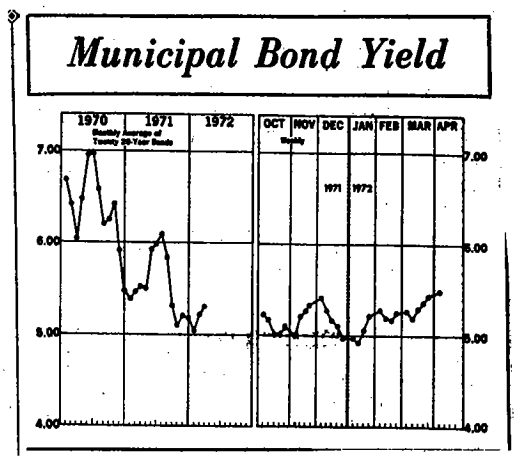


On a mechanical basis, a bull signal was rendered last week as the Industrial Averages, following its 1971 plunge from the April peak of 950.82, rallied back and bettered the 950.82 high. In so doing, Industrials confirmed the much earlier advance by the Transportation Average above its own April, 1971, peak of 232.79. All of this is shown on the weekly chart at right.

I do not (despite the protestations of almost all my colleagues) consider these movements as "confirmation of a new bull market." I would say that all of the 1971 action represents a normal upward correction of the 1969-70 collapse. The action of 1972 I would consider an "over-correction" brought on by Government policies which have gone beyond anything which has ever been seen or envisioned in this nation.

Again referring to the weekly chart at right, it is notable that the advance-decline ratio has formed a 1972 peak far below the April, 1971, peak, and the most recent rally (which took the Dow to new recovery highs) has failed to take the A-D ratio even above its preceding 1972 peak. This action has resulted in a definite non-conformation on the part of the A-D ratio, and it will be important to see whether the market can muster enough breadth over the period ahead to at least take the A-D ratio above its 1972 peak.

As to the fantastic Government stimulation of 1971-72, nothing is attained without a price. And the repercussions of the 1971-72 follies are beginning to appear. We see one on this chart of tax-free municipal bond yields. The bond yields have just traced out an upward zig-zag which means that tax-free yields are heading back to the 6% zone again. In other words, one by one the problems of 1966 to 1971 will be rekindled. It is simply a matter of whether Mr. Nixon can slip by the 1972 elections with the bullish banner still waving, or whether the closet full of troubles will prove too weighty to be held in check at the convenience of the President of the United States.



On April 5 the New York Times took cognizance of the interest rate situation, and I reproduce the beginning of this article on page 3. It should also be remembered that stock yields are currently near historic lows, and this fact together with climbing interest rates for bonds makes for a tenuous situation on the equity markets.

BIG PICTURE: On April 4 the Transports (mainly due to strength in airlines) jumped over 6 points to close above their March 9 peak (262.62) at a new recovery high for the entire rise since 1970. Spurred by this spectacular performance in Transports, the Industrial Average on April 5 hurdled its own March 6, 1971, peak of 950.18, to close at 954.55. In doing so, Industrials also bettered the more important April, 1971, high of 950.82, a mark which they had been flirting with for the past four months.

In order to put the entire picture into perspective, I have included my weekly, semi-logarithmic chart of the three Dow Averages, going back to 1966. Since semi-log or ratio scale shows all movements in percentages, the relative strength of the three Averages can be properly compared on this chart.

With their leveraged (high debt) financial structures, the Transports constitute by far the most speculative of the three Averages. Thus the collapse in Transports from the 1969 peak of 279.88 to the 1970 low of 116.69 erased 59% of the value of that Average. In comparison, Industrials from their 985.21 peak of December, 1968, to their 631.16 low of 1970, lost 36% of their value. By the same token, the rise since the 1970 lows was greater for Transports than Industrials, and last week's closing found the Transport segment within points of their 1969 all-time record high of 279.88.

As seen on the chart, this is not true of Industrials, which, having hurdled the 1971 peak of 950.82, still have the 1968 high of 985.21 and the 1966 high of 995.15 to negotiate. Thus, we are left with a most interesting picture as the market enters crucial territory and as the Industrial Average moves within 50 points of its 1949-66 bull market high. As seen on the

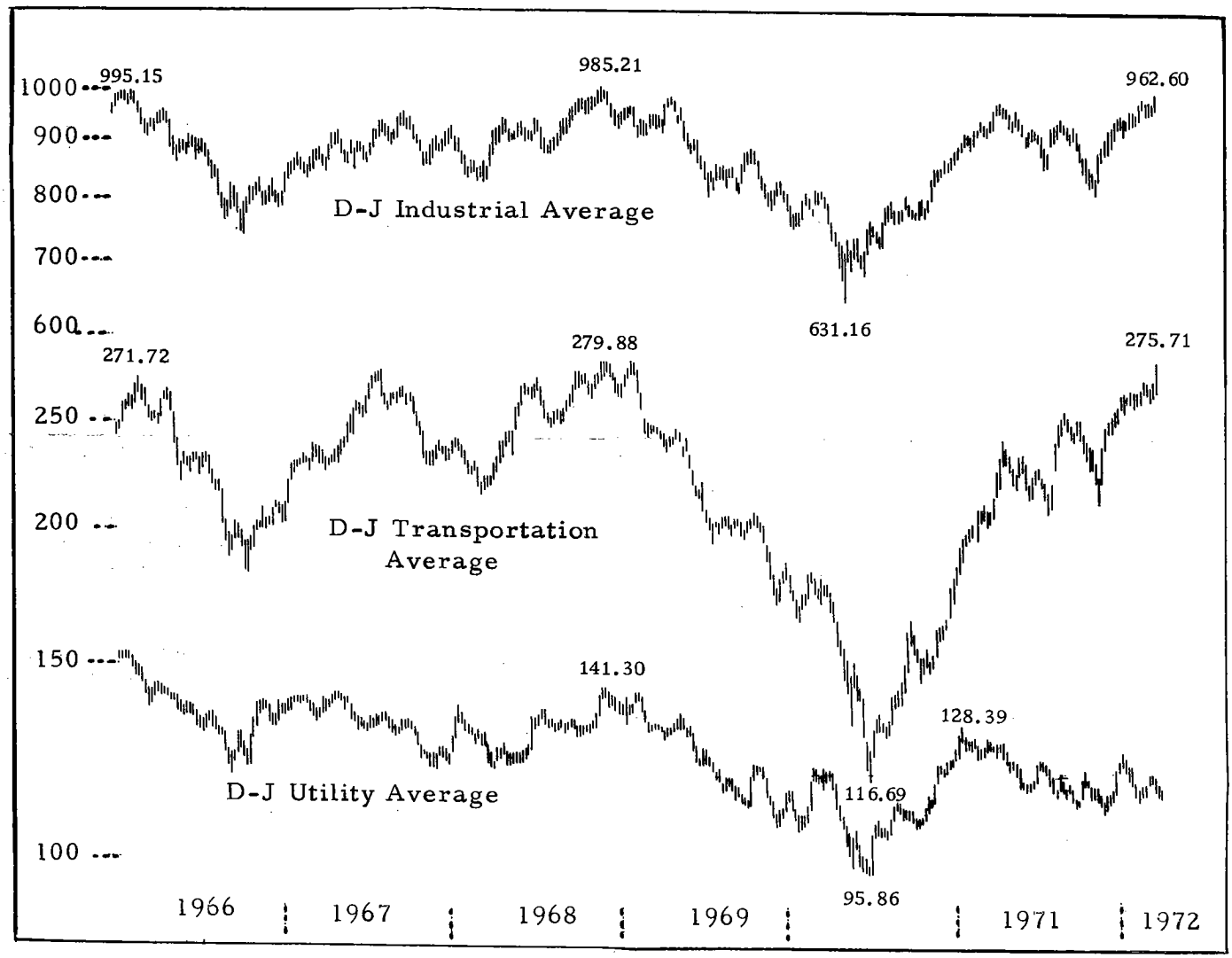
BEARS PROWLING CREDIT MARKETS

Upward Sweep of Interest Rates Gaining Momentum Throughout All Sectors

By ROBERT D. HERSHEY Jr.

Credit Markets

The upward sweep of interest rates gathered renewed momentum yesterday, as bearish sentiment regarding the money and capital markets spread into all corners of the investment community. Virtually all rates—on securities coming due in a few days up to those maturing in the next century—showed some kind of increase. Among the principal developments were these:

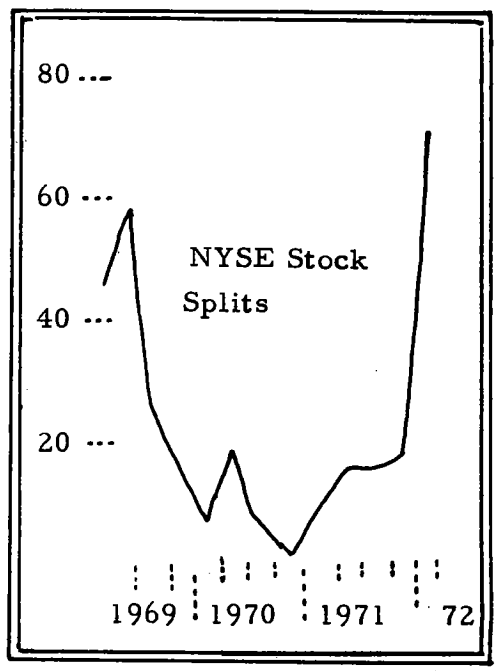


chart, the 950-995 area has stopped the Industrial Average on all advances over the past six years or since February, 1966. This 950-995 area, in fact, has been one of massive distribution each time the Industrials have entered it. How do we know distribution has occurred on every rise into 950-995? Because following each rise into that area, Industrials (and the entire market) have fallen badly, first in 1966 (following the 995.15 peak), then in 1969-70 (following the 985.21 top), and most recently during 1970-71 (following the 950.82 top).

What is in store for the market now, with Industrials in the same territory in which they have previously "struck out" three times in a row? That mystery remains to be seen, and if nothing else, it virtually guarantees an exciting picture for the rest of 1972. I doubt very much whether the senior Average will languish very long in the 950-995 area, and the measure of the struggle will be the amount of volume churned up in the 45-point zone between 950 and 995. Personally, I would guess the story will be told within the next few months. A push above 985.21, then 995.15, would probably stir up some of the greatest volume of trading ever seen on the Exchange, and (I believe) some very deceptive, yet spectacular action. Conversely, a break below the 900 level would most likely signal a major collapse with the great primary bear market (which has held the Dow under the 1966 high for six years) moving into full force again.

As for the Utility Average, which has been in a downtrend ever since the 1965 high of 163.32, this investment-grade index seems to have hit its primary bull market peak and is merely marking time while the other Averages put on the show. As a rule, the Average which lags on the general advance is the one which leads on the next decline. For this reason, I would say that Utility shares are very vulnerable to collapse as soon as this market turns down. Therefore, this would be the best area to liquidate stocks in the Utility field. It is notable and surprising that the Utility Average (despite its vaunted "defensive" character), lost a full 40% of its value on its decline from the 1965 high to the 1970 low. Currently, the Utility Average is only 18% above its 1970 low of 95.86.

OUT THEY GO: In the last Letter I included a chart showing the record number of secondary distribution on the N.Y.S.E. for the month of March. This indicated that large interests were taking advantage of 1972's huge volume and speculative excitement to get rid of stock via the secondary route. During poor markets (refer to last week's chart), secondary offerings dwindle off to practically nothing, as at the 1966 or 1970 bottom.



Another indication of distribution is the stock "split." Although most companies that split their shares state that they are doing so in order that the shares obtain "wider distribution," I would say that the stock split is simply a way of distributing the stock to the public via the excitement of a suggested "something for nothing." One week the buyer has 100 shares, and a week later (after the split) the same buyer has a magical 200 or 300 shares, depending on the split. This usually allows room for the stock to move higher, since the public is used to a certain price range for the stock. If the public sees the "new" split stock at half the old price, the issue "looks cheap," and the buyers may push a bit higher than it would have otherwise gone.

In 1969 a record 147 stock splits were announced on the N.Y.S.E., and this occurred at or near the top of 985.21. But a year later, in 1970 (when the market was tumbling down) stock splits on the Big Board dropped to 38. Then in 1971 the splits rose to 66, a big jump over 1970. But this year the figures are really startling. In the first three months of 1972, 72 companies on the N.Y.S.E. have either split their shares or announced splits. On an annualized basis this would suggest about 290 splits for the year. A total of 290 would represent a 100% jump over record 1969, and it would fit in with the current record spate of secondary distribution.

My conclusion is that stocks are being distributed to the public for all they are worth by every device known to Wall Street. Of course, such indication cannot pin-point a top — nothing can. But they suggest that we are in a top area, and that large interests know it and are using the vehicles open to them — to get out.

WORLD PICTURE: Few people are aware of the vast changes in the international economic picture which have taken place since World War II. Study some of the statistics listed below.

Percentage of total in the world's GNP...

	1950	1970	change
United States	39.3	30.2	-9.1
Common Market	11.1	14.8	+3.7
Japan	1.5	6.2	+4.7

Industrial production index, 1960-70 period (1960 equals 100)

United States	161
West Germany	176
Japan	370

International reserves (gold, SDR's, IMF reserve position, foreign exchange) in percentages of total world reserves.

	1950	1970	change
United States	49.8	10.6	-39.2
Common Market	6.1	32.9	+28.6
Japan	0.6	10.9	+10.3

In the current issue of Fortune there is an article which notes that the U.S. is now lagging behind other nations in technology, and there is no question about it, in many new areas, business is being taken away before the U.S. ever get started in it. Another reason for the U.S. losing business is price inflation, and the fact is that many overseas nations are now producing products which are as good or better than U.S. counterparts and sold for considerably less. A third reason why the U.S. is losing out in world markets is simply the superior quality of many foreign products. This is particularly ironic since prior to World War II anything foreign (with the exception of Swiss or German workmanship) was considered "junk." Not so today, and many foreign products are now sold not only on the basis of price competition but quality competition (does anyone believe the VW and Datsun compete with U.S. autos on the basis of price alone?).

This foreign "invasion" of U.S. markets is a wave that is getting bigger but one that is to a large extent obscured in the tides of U.S. deficit financing. Awash in an ocean of fiat dollars, the American consumer is becoming totally exasperated with the financial situation, and his "old fashioned" hope of having a nest egg or "savings for a rainy day" has gone the way of the dinosaur. This has given way to two disparate trends.

One trend is towards the "spend now, pay later" syndrome, wherein the spender just wants the material goodies of life now, and if in a year his job is gone, well, he at least had fun while it lasted. Along these lines, personal bankruptcies keep climbing, and more and more Americans spend themselves broke, then give it all away as the piper is paid.

The other trend is "back to the earth," and "I don't want to own anything or be a slave to the system." This has given rise to a whole new ethic on the part of a large segment of our youth. It has given birth to the "drop-out sub-culture," and it has actually led to whole new trends in American life such as backpacking, communes, organic food, ecology, and unfortunately, drugs.

I include this interesting set of figures (courtesy of Macro Publishing Co., N.Y.C.) which shows how we make more money today, pay more taxes today, are hit harder by inflation today, and end up with less spending power for all our trouble and anxiety.

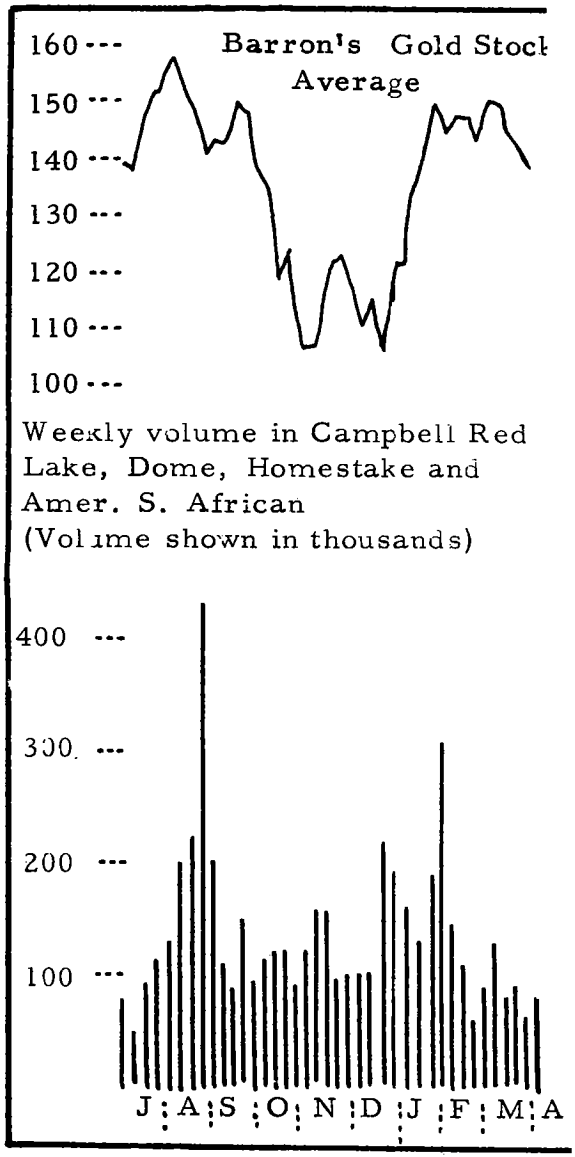
IF YOUR 1966 SALARY WAS:	AND RAISES MAKE YOUR 1972 SALARY:	YOUR TAXES IN 1972 WILL BE HIGHER BY:	INFLATION WILL CUT YOUR 1972 INCOME BY:	AND YOUR 1972 BUYING POWER WILL BE SMALLER THAN '66's BY:
$10,000	$13,000	$698	$2,421	$119
20,000	26,000	1,660	4,610	270
30,000	39,000	3,157	6,542	699
40,000	52,000	4,968	8,247	1,215
50,000	65,000	6,917	9,783	1,700

I have never seen or heard of a society which survived and which accepted the current thesis that "a little inflation each year is all right." At a 6% rate of inflation (which is the annualized inflation figure now existent in this nation, based on last month's reading of the Consumer Index) the purchasing power of the dollar is cut in half in twelve years. Does anyone think we can go on at this rate of decay and erosion of savings and purchasing power?

No wonder Americans are turning almost in desperation to the stock market as a place where they can throw their depreciating fiat dollars in an attempt to hold off the disease of inflation. The results in this type of situation have always been the same. Wild speculation, the fall of morality and the fall of the currency, and finally the fall of the society itself. Maybe this time it will be different; let's hope so.

GOLD: In the last Letter I wrote quite a bit about the evolving gold picture, and the question arises, "How can we tell when the U.S. market is going to go for the gold shares?" One of the indicators I watch in attempting to gauge the gold picture is the volume in the four listed gold shares on the N.Y.S.E. (American South African Investment Trust and Dome are actually holding companies, but I include them under the general category of gold stocks along with Campbell Red Lake and Homestake),

The accompanying chart shows the weekly volume in the four listed gold stocks together with Barron's Gold Stock Average for the period of July, 1971, to the present. If you glance at the Market Laboratory page of Barron's, you will notice that volume in the last or twentieth most-active stocks for any given week runs from about a quarter to a half million shares. In contrast, volume in all four listed gold shares did not run as high as half a million shares for any week since this chart was started. During one week in August, 1971, volume went over 400,000 shares, and for a single week in January volume expanded to over 300,000 shares, but in general volume in the only listed gold shares on the Big Board runs around 100 to 200 thousand shares per week, this despite all the excitement of 1971 and 1972 and despite the first dollar devaluation since the 1930's.



What is the conclusion? Well, my conclusion is that the public, so far, is singularly disinterested in gold shares. Strangely, the public is interested in gold, and gold sales in jewelry and general talk of gold was never more widespread. But as for purchases of gold stocks, the public simply is not in the picture.

However, I would guess that the picture is going to change within the next few years. This would mean to me that we can expect a definite large increase in the volume of gold shares traded, rather than the paltry 60 to 100 thousand shares which go by on the N.Y.S.E. on my average weeks.

Actually, I have a "signal" in my mind regarding the gold shares. That signal consists of four weeks in a row when gold share volume among the four listed gold stocks rises to half a million shares or better. Such action, I believe, would signal a great rise coming in gold stocks and the entrance of the public on the scene. Meanwhile, I consider the golds on the "bargain counter" with the public totally disinterested in the equities.

GOLD PRICE: From the April 11 Christian Science Monitor by Business Editor Richard Nenneman (Article entitled "Some European Views of the Monetary Crisis"):

Paris

He was the exchange trader, a Frenchman, for an American bank in Paris. He rushed into the room, half an hour late. He apologized. He had just worked out a major currency deal. (France currently has a double rate for the dollar, which complicates business here.)

"How would you react if there were another dollar crisis?" I asked.

"Another one? We are still in the same one." he flashed back.

As if sensing what the Frenchman above sensed, the price of gold in London shot up 40¢ on April 12 to close within a fraction of its historic February peak. This is shown on the daily gold chart on this page. I would consider a "breakout" above $49.50 as the signal for a new and perhaps important rise in the market price for the yellow metal.